



DEPARTMENT OF THE TREASURY  
INTERNAL REVENUE SERVICE  
WASHINGTON, D.C. 20224

TAX EXEMPT AND  
GOVERNMENT ENTITIES  
DIVISION

Release Number: **200708086**  
Release Date: 2/23/07  
Date: November 30, 2006  
UIL: 507.00-00

Contact Person:

Identification Number:

Telephone Number:

Employer Identification Number:

Legend:

Y =  
Z =  
A =  
B =  
C =

Dear :

We have considered the request of Y and Z, dated August 16, 2005, for a ruling concerning the federal income and excise tax consequences of a proposed transfer of one-half of Y's net assets to Z.

Facts:

A incorporated Y in 1955 and incorporated Z in 2005. Both organizations are recognized as exempt from federal income tax under section 501(c)(3) of the Internal Revenue Code and are private foundations under section 509(a). A has two sets of four grandchildren, the B grandchildren and the C grandchildren. Currently, A and one member of each of the two sets of grandchildren control Y.

A's grandchildren have developed diverging charitable interests, so A proposed that Y transfer one-half of its assets, comprised of corporate stocks and bonds, to Z. After the transfer, A and the B grandchildren will control Y, and A and the C grandchildren will control Z.

Both Y and Z state that they will make grants to organizations that are exempt under section 501(c)(3) of the Code. Y states that it will continue its charitable activities, does not intend to terminate, and has never participated in an act or activity that would give rise to liability under Chapter 42 of the Code. Y represents that its assets do not constitute excess business holdings

as described in section 4943 and has promised to exercise expenditure responsibility with regard to the transferred assets and has drafted a written agreement that will ensure that Z will use the transferred funds properly.

You have requested the following rulings:

1. The transfer of assets will not affect the tax-exempt status of either of the foundations under section 501(c)(3) of the Code.
2. The transfer of assets will qualify as a transfer under section 507(b)(2) of the Code.
3. Y will neither terminate nor incur a termination tax on the transfer under section 507(c) of the Code.
4. Y will not incur an excise tax on net investment income under section 4940 of the Code due to the transfer of assets.
5. The basis of the assets received in the transfer by Z will be Y's basis in the assets.
6. The transfer will not be an act of self-dealing under section 4941 of the Code.
7. Y will not incur a tax on undistributed income under section 4942 of the Code.
8. Y will not incur a tax on excess business holdings on the transfer under section 4943 of the Code.
9. The transfer will not constitute an investment that jeopardizes Y's exempt purposes under section 4944 of the Code.
10. The transfer and the reasonable and necessary expenses in making such transfer will not constitute taxable expenditures under section 4945 of the Code, provided appropriate expenditure responsibility requirements are satisfied.

Law:

Section 501(c)(3) of the Code exempts organizations that are organized and operated exclusively for charitable and other exempt purposes from federal income tax.

Section 507(a)(1) of the Code states that the status of any organization as a private foundation is terminated only if it notifies the Secretary of its intent to terminate or there have been either willful repeated acts or a willful and flagrant act giving rise to liability for tax under chapter 42 and the Secretary notifies the organization that it is liable for termination tax under section 507(c).

Section 507(b)(2) of the Code permits one private foundation to transfer its assets to another private foundation without treating the transferee foundation as a newly created organization.

Section 507(c) of the Code imposes a tax on a private foundation that terminates its private foundation status by notifying the Service of its intent to terminate or that has made willful, repeated acts (or failures to act), or a willful and flagrant act (or failure to act) that results in tax under Chapter 42, and the Service has notified the organization that it is liable for the tax and either the organization has paid the tax or the tax was abated.

Section 509(a) of the Code describes exempt organizations that are exempt from federal

income tax under section 501(c)(3) and that are private foundations.

Section 4940 of the Code imposes an excise tax on certain net investment income of private foundations.

Section 4940(c)(1) of the Code defines net investment income as the amount by which the sum of the gross investment income and the capital gain net income exceeds the allowable deductions.

Section 4940(c)(2) of the Code defines gross investment income as the gross amount of income from interest, dividends, rents, payments with respect to securities loans, and royalties.

Section 4941 of the Code imposes an excise tax on acts of self-dealing between a private foundation and its disqualified persons as described in section 4946.

Section 4942 of the Code imposes a tax on the undistributed income of a private foundation for the taxable year. It requires a private foundation to pay annual qualifying distributions, as defined in section 4942(g), to accomplish one or more exempt purposes. A “qualifying distribution” includes any amount paid to accomplish one or more purposes described in section 170(c)(2)(B).

Section 4943 (a)(1) of the Code imposes a tax on the excess business holdings of a private foundation during the tax year.

Section 4944 of the Code imposes a tax on any investment that jeopardizes an exempt organization’s charitable purpose.

Section 4945(a) of the Code imposes a tax on the taxable expenditures of a private foundation.

Section 4945(d)(4) of the Code defines the term “taxable expenditure” as any amount paid or incurred by a private foundation as a grant to an organization unless the organization is described in paragraph (1), (2), or (3) of section 509(a) or is an exempt operating foundation, or the private foundation exercises expenditure responsibility with respect to the grant.

Section 1.507-1(b)(6) of the Income Tax Regulations states that a transfer of assets made by a private foundation, as described in section 507(b)(2) of the Code, does not constitute a termination of the transferor foundation’s private foundation status under section 507(a)(1).

Section 1.507-3(a)(5) of the regulations requires a private foundation to meet the distribution requirements of section 4942 for any taxable year in which it makes a section 507(b)(2) transfer of all or part of its net assets to another private foundation under section 507(b)(2) of the Code.

Section 1.507-3(a)(7) of the regulations provides that where the transferor has transferred all of its assets, during any period during in which the transferor has no assets, section 4945(d)(4) and (h) shall not apply to the transferee or the transferor with respect to any “expenditure responsibility” grants made by the transferor.

Section 1.507-3(a)(8)(ii)(a) of the regulations states that the tax basis and holding period of the assets will carry over to the transferee foundation for purposes of section 4940(c)(4)(B) of the Code.

Section 1.507-3(a)(9)(i) of the regulations states that if a private foundation transfers all of its net assets to one or more private foundations which are effectively controlled by the same person or persons which effectively control the transferor private foundation, for purposes of Chapter 42 and part II of subchapter F of chapter 1 of the Code, such a transferee private foundation shall be treated as if it were the transferor.

Section 1.507-3(c)(2) of the regulations defines the term "significant disposition of assets to one or more private foundations" as any disposition or series of dispositions where the cumulative total of dispositions is 25 percent or more of the fair market value of the net assets of the foundation at the beginning of the taxable year.

Section 53.4945-6(b)(2) of the Foundation and Similar Excise Taxes Regulations provides that a private foundation's payment of administrative expenses, including compensation, consultant fees and other fees for services rendered is not a taxable expenditure depending upon whether such expenses are reasonable.

Section 53.4946-1(a)(8) of the regulations states that, for purposes of section 4941 only, the term "disqualified person" shall not include any organization which is described in section 501(c)(3).

Analysis:

The proposed transactions involve a private foundation's transfer of a significant part of its assets to an entity that qualified for exemption under section 501(c)(3) of the Code and not a notification of its termination as a private foundation. Accordingly, the proposed transfer is not a transfer described in section 507(a) of the Code which is subject to tax under section 507(c). Also, because Z is exempt under section 501(c)(3) of the Code, the transfer of Y's assets to Z will constitute a distribution for a charitable purpose and will not adversely affect the exempt status of Y or Z, nor will it be treated as investment income, an act of self-dealing, a jeopardizing investment or taxable expenditure within the meaning of sections 4940, 4941, 4944 and 4945. In addition, Y's payment of reasonable expenses incurred in connection with the transfer will not be treated as acts of self-dealing under section 4941 or taxable expenditures under section 4945.

Based on the foregoing, we rule, as requested, as follows:

1. The Transfer is a transfer described in section 507(b)(2) of the Code.
2. Because the Transfer is a transfer described in section 507(b)(2) of the Code:

- a. The Transfer shall not affect Y's qualification as an organization described in section 501(c)(3) of the Code;
  - b. Z will not be treated as a newly created organization as provided in section 507(b)(2) of the Code and section 1.507-3(a)(1) of the regulations;
  - c. Z will succeed to the aggregate tax benefit of Y in proportion to the assets transferred to it by Z as provided in section 1.507-3(a)(2) of the regulations;
  - d. If Y incurs liability for any taxes imposed by Chapter 42 (or any penalty resulting therefrom) prior to, or as a result of, the Transfer, in any case where transferee liability applies, Z shall be treated as receiving the transferred assets subject to such liability to the extent that Foundation does not satisfy such liability as provided in section 1.507-3(a)(4) of the regulations;
  - e. Y will be required to meet its distribution requirements for the year or years in which the Transfer takes place in accordance with section 1.507-3(a)(5) of the regulations; and
  - f. The provisions of sections 1.507-3(a)(8)(ii)(a) through (g) of the regulations will apply to Z with respect to the assets transferred from Z.
- 3. The Transfer will not cause the termination of Y's status as a private foundation.
  - 4. The Transfer will not cause the imposition of a termination tax under section 507(c) in the year or years in which the Transfer takes place.
  - 5. The Transfer will not give rise to net investment income for either Y or Z and will not result in the imposition of tax under section 4940(a) of the Code.
  - 6. The Transfer will not constitute an act of self-dealing under section 4941 of the Code for Y or Z.
  - 7. The Transfer will not constitute a jeopardy investment under section 4944 of the Code with respect to Y or Z.
  - 8. The Transfer will not constitute a taxable expenditure under section 4945(d)(4) of the Code as Y will exercise expenditures responsibility under section 4945(h) with respect to its transfer to Z.
  - 9. The payment or reimbursement by Y of all the transfer and related expenses, if reasonable in amount will not constitute taxable

expenditures within the meaning of section 4945 of the Code.

This ruling will be made available for public inspection under section 6110 of the Code after certain deletions of identifying information are made. For details, see enclosed Notice 437, Notice of Intention to Disclose. A copy of this ruling with deletions that we intend to make available for public inspection is attached to Notice 437. If you disagree with our proposed deletions, you should follow the instructions in Notice 437.

This ruling is directed only to the organization that requested it. Section 6110(k)(3) of the Code provides that it may not be used or cited by others as precedent.

If you have any questions about this ruling, please contact the person whose name and telephone number are shown in the heading of this letter.

Sincerely,

Debra J. Kaweck  
Manager, Exempt Organizations  
Technical Group 2

Enclosure  
Notice 437